LCP powering possibility

Chart your own course

Taking control of your journey: results of our 2024 survey of DB pension schemes

June 2024

Taking control of your journey

It's better to be proactive rather than reactive.

With the past 12 months offering relative calm after the turbulence of the last few years, as well as a (relative) slowdown in pensions regulatory change, this year's annual DB pension scheme survey showed that schemes have used their time effectively.

We've seen schemes taking positive actions in a range of areas, from endgame planning to net zero targets to Diversity, Equity & Inclusion (DEI).

Of course, it hasn't all been good news and our survey showed that risks such as cyber, AI and fears of another gilt market event remain front of mind for many respondents. But encouragingly, schemes have been taking actions to prepare themselves in these areas too.

As usual, this year's Chart your own course report contains insights from our recent survey of the pensions industry. Thank you, if you responded – as well as providing us with valuable information, each completed entry prompted a £5 contribution to The British Red Cross. As ever, we also use data on our own client base derived from our flagship asset and liability tool LCP Visualise to show trends in positions and activity across the year. We hope you enjoy exploring this year's findings.

After many years of mixed news, it feels like the last year has generally been really positive for DB schemes. Funding positions continue to improve, and it was great to see our survey results showing that so many schemes have been taking positive actions in areas from endgame, to climate risk, to Diversity, Equity & Inclusion. We're seeing schemes really taking control of their journey.

Jon Forsyth
Partner and Lead Author

Key insights from this year's report

Funding positions continued to improve

In last year's report we saw big improvements in funding positions off the back of gilt yield rises – and this year has generally seen further improvements.

Over the year to 31 March 2024 **more than one third of schemes saw funding levels improve by 5% or more** on a gilts flat and buyout basis.

And although improvement wasn't universal, **fewer than 10% of schemes saw their position get worse.**

An impressive **30% of schemes** are now fully funded on buyout – **up from 20%** in our 2023 analysis.

Source: LCP Visualise

Endgame options are growing, but risk transfer remains a top priority

Despite such high funding levels, not all schemes who can afford to insure want to, and we are seeing more examples of well-funded schemes considering alternatives like active run-on. But when asked about their top priority for the coming year, the most popular answer amongst our survey respondents was still completing a risk transfer transaction.

Net zero targets have become the norm

Our survey showed that more and more schemes are taking positive action on climate risk. Amongst schemes over £5bn, **90%** now have a net zero target or are working through the practicalities. But medium and smaller schemes are also taking steps – the equivalent figure for schemes in the £500m-£1bn range is **over 60%**, and **almost 40%** for schemes below £500m.

What's in this report

As in previous years, we have built our report around the LCP GEARS framework, and how it can help you design your Strategic Journey Plan to achieve your chosen endgame. In each section we build on the issues mentioned below, cover the results from our survey and share our experiences.

G — Get the right governance structure in place

The right governance structure can be different for each scheme, but good decision making and an inclusive environment are always key. We look at where the industry is on tackling DEI issues.

Page 4

E — Establish your endgame and timescales

Knowing your ultimate target helps frame all strategic decisions, particularly with an increasing range of options available. We summarise where schemes are heading and the different endgame options targeted.

Page 5

A — Analyse what could change your journey

Covenant remains an important risk for many schemes but is certainly not the only one. We look at how schemes are thinking about covenant, but also systemic risks that could impact the whole industry, with a spotlight on cyber risk.

Pages 6 - 8

R — Refine the steps you plan to take to reach your goals

Your journey is driven by sponsor contributions and your funding and investment strategy, but also what members choose to do with their benefits, and the options and support you give them. We look at latest investment trends as well as progress on member-led activities.

Pages 9 - 11

S — Steer your journey dynamically and in a joined-up way

Every journey is different, but planning for different scenarios and reacting quickly are always important. We look at why schemes have been changing direction, and top priorities for the coming year.

Page 12

Additonal steps where relevant

Transact successfully and at the right time

For those targeting full insurance, preparation and timing are paramount. We look at planned timescales for transactions and what approach schemes might be taking.

Page 13

Complete wind-up effectively

Securing all benefits with an insurer is a momentous occasion, but is not the end of the road. We offer top tips to make sure the end of the journey is a success.

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Additional resources

Relevant material at your fingertips

Access links to further reading on many of the topics covered in this report, and some of our recent webinars.

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Our survey

Find out more about our survey participants and the questions we asked.

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Our experts

Find out who to contact to learn more.

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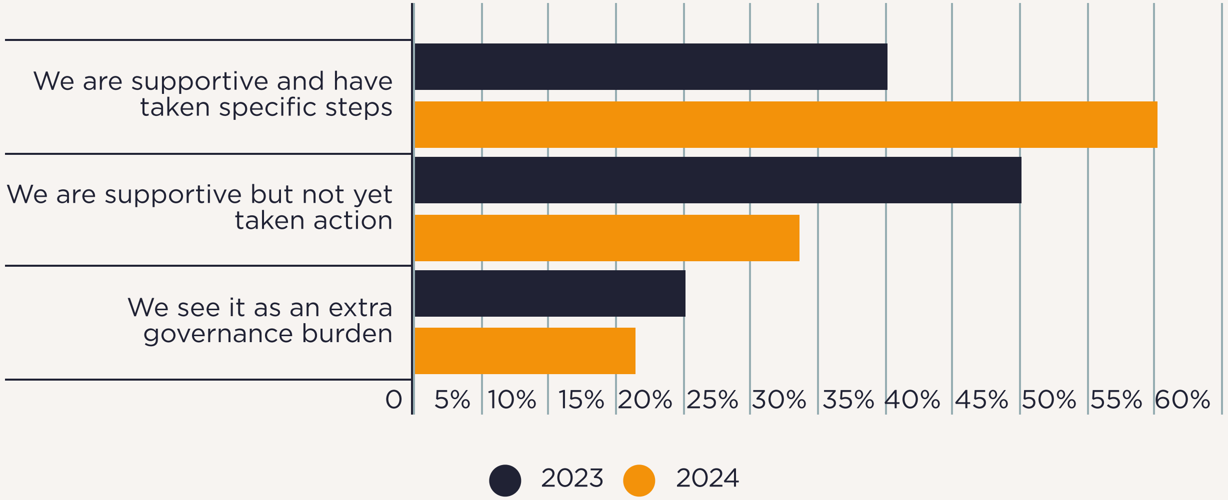
Progress is being made on DEI

What action are you taking in relation to DEI issues?



> *It's really encouraging to see that the majority of schemes have now taken specific steps on DEI issues. At LCP we're proud of our DEI journey so far and of the work we have done to help our clients in this area. Although challenges remain, it's great to see the industry taking positive action.*

Jill Ampleford
Partner and Head of Trustee Consulting

Good practices on DEI support better decision-making and understanding of the diverse needs of pension scheme members.

That's why we were so pleased to see that a much greater proportion of respondents this year told us they have taken specific action in respect of DEI issues, and in fact such schemes are now the majority.

The largest schemes are leading the way here with almost 80% of schemes over £5bn having taken specific steps, but encouragingly the proportion was at or around 50% of schemes for all size categories from our survey, including schemes under £500m.

These steps can be small – perhaps as simple as refreshing member communications to use more inclusive language or updating trustee selection processes to encourage a more diverse set of applicants – but can have a material impact.

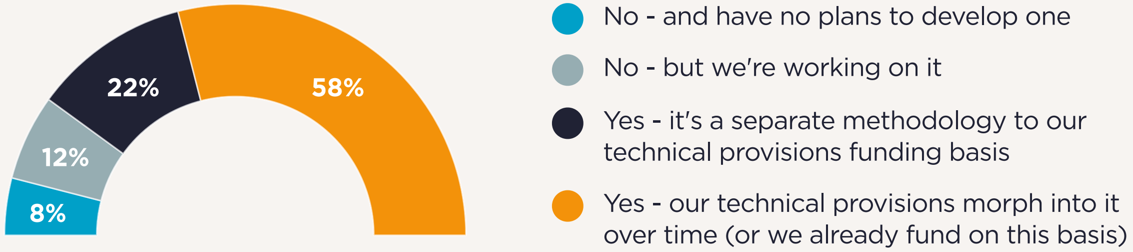
A further significant minority (c30%) remain supportive but have not yet taken action – we hope they continue the momentum of others and the trend carries on in this direction!

Curious?

+ **Check out our Trustee DEI guide to learn more about where to start on these issues, or contact LCP Partner Zoe Burdo to understand how we can support your journey in a practical and pragmatic way. You can also read about LCP's DEI journey.**

Schemes are thinking hard about their endgame

Do you have a long-term low dependency funding target?



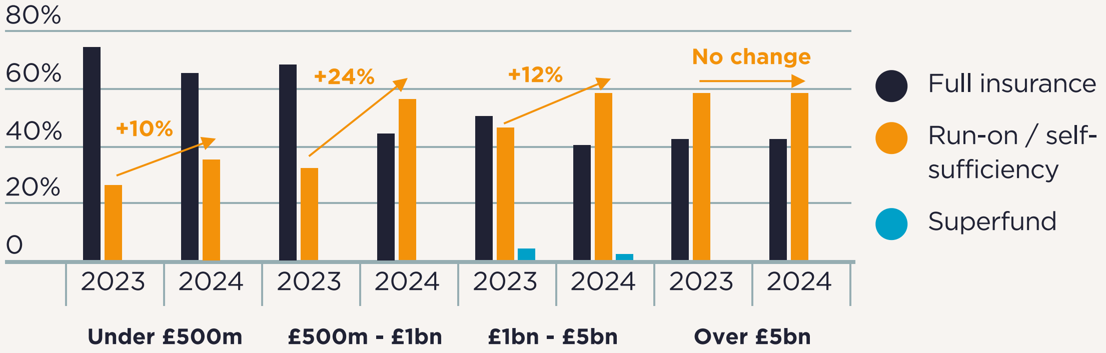
As in previous years, our survey showed that the vast majority of schemes either already have or are working towards a low dependency funding target.

Although for many this will just be a stepping stone to their ultimate endgame or a longer-term objective, it is an important part of TPR's new funding regime – and so any schemes who do not already have a low dependency target should have it on their agenda for the coming months.

> *Many more schemes are now exploring the full range of endgame options rather than assuming insuring as soon as affordable is the right answer. Although insurance will still be right for many, for those looking to run-on there is lots of innovation in the market to help protect members and the potential rewards for all stakeholders are huge.*

Jonathan Griffith
Partner and Head of Endgame Innovation

What is the long-term objective for your scheme?



For the smallest schemes it was no surprise to see full insurance remain as the most popular endgame. However it was interesting to find that especially amongst medium-sized schemes, self-sufficiency or active run-on are becoming noticeably more popular, as schemes start to think about the range of options available to them. For schemes over £500m, these run-on options are now more popular than full insurance. Of course, these options are not binary and many schemes looking at run-on will ultimately still look to buyout at some point in the future. In practice, some larger schemes use buy-ins as part of a run-on strategy.

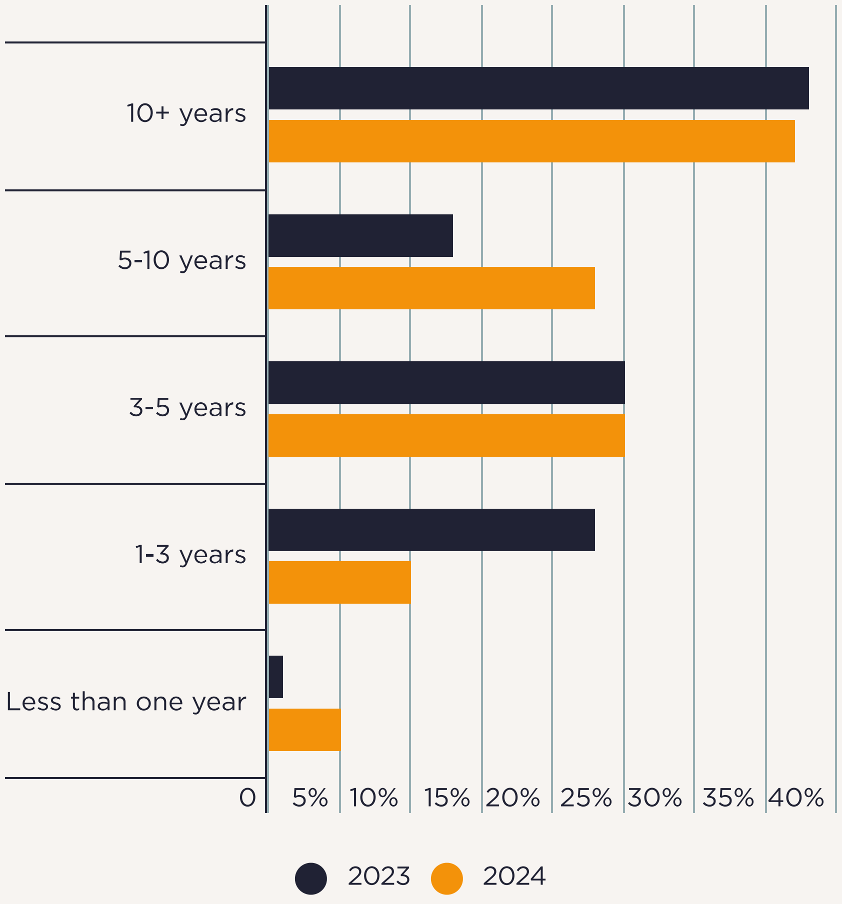
Targeting superfunds currently remains much rarer, but they can offer a valuable option for schemes in the right circumstances, and interest may increase following the first DB superfund transfers.

Curious?

+ Find out more about endgame and journey planning here.

Is your covenant as reliable as you think?

How long do you think your employer covenant is reliable for?



For many schemes, covenant remains the most important risk, and so it's no surprise to see its importance and prominence increasing in TPR's new DB funding regime.

A new and very important concept in that new regime is covenant "reliability" – this is the period of time over which trustees can be reasonably confident about the level of the employer's available cash to fund the scheme into the future.

TPR has said that it expects in most cases the reliability period to be no more than six years, so it was interesting to see that over a third of respondents to our survey were confident that their covenant was reliable for 10 or more years. It remains to be seen what evidence TPR will expect in these cases, should trustees wish to incorporate a longer reliability period into their funding & investment strategies.

At the other end of the spectrum, 15% of schemes thought their covenant reliability period was less than three years or one valuation cycle – with one third of those believing it to be less than a year. For these schemes, understanding what is affordable for their sponsors and whether any alternative support could be made available will be high on the agenda.

Curious?

+ Get in touch with our covenant team to stay ahead of the new requirements.

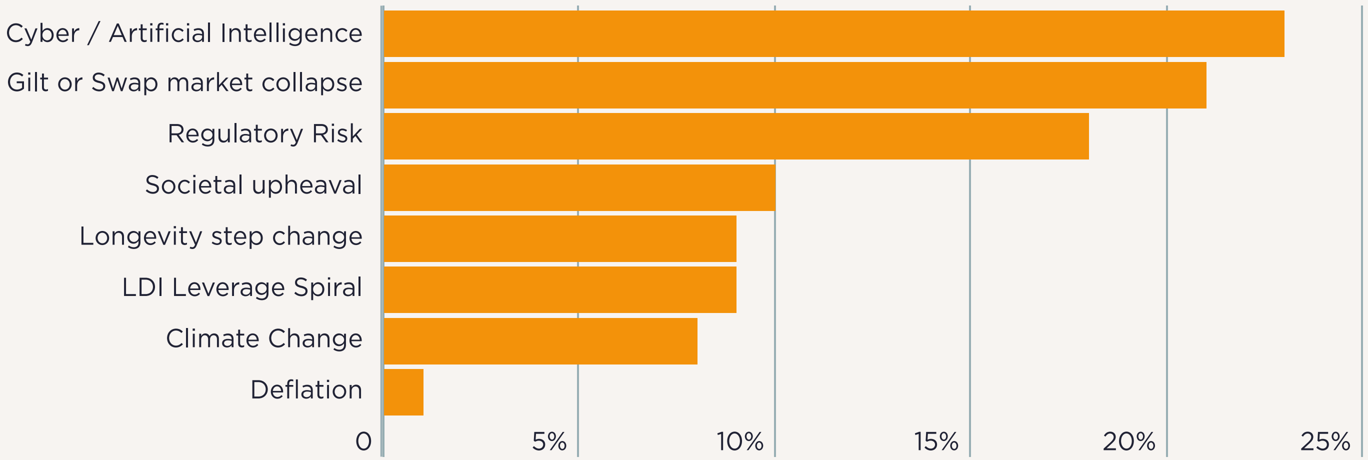
Even when schemes are well funded the employer covenant remains important to bridge the gap to endgame and ensure that members get the pensions they have been promised. We're expecting TPR to ask all trustees about their covenant reliability period, and it will likely request evidence where this is longer than six years, so trustees should document their considerations.

Helen Abbott
Partner, Covenant

Systemic risks

Systemic risks are those that cannot be diversified away as they do not just affect one company or holding, but instead can have a broader impact on the wider economy.

Of the following systemic risks which are you most worried about for your DB scheme?



When asked to rank systemic risks in the order they are most worried about for their schemes, Cyber and the risk posed by Artificial Intelligence was the category most often selected as the top worry for respondents.

It was noteworthy to see gilt market collapse and another (accompanying?) LDI leverage spiral ranking so highly among this menu of risks. The idiom of "once bitten twice shy" certainly comes to mind when viewing these results and is a stark reminder that not all schemes came through the 2022 gilts crisis unscathed.

At the opposite end of the scale, it was surprising to see climate change with few selections, and only a sole vote for deflation. Though with market expectations for inflation now remaining higher for longer relative to when our survey question was asked, perhaps our respondents knew something others didn't!

The actions taken by pension schemes since 2022 to increase the resilience of their LDI collateral has significantly reduced the risk of another gilts crisis occurring. However, the risk of a collateral stress event has not gone away, so trustees will need to monitor their specific position carefully going forward.

Gavin Orpin
Partner & Head of Investment Strategy

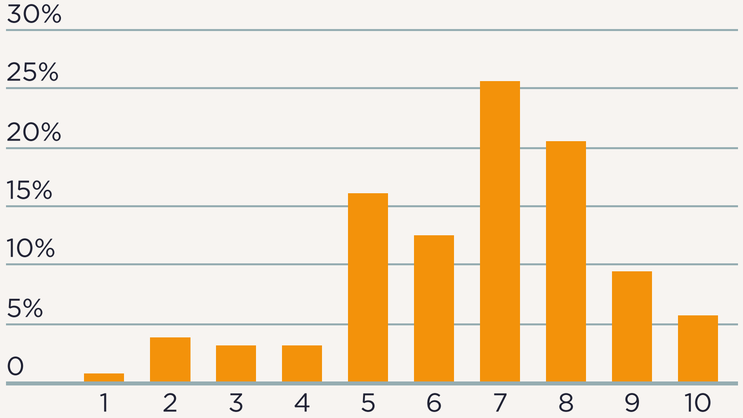
Curious?

+ **Speak to your LCP contacts about systemic risks and if you could benefit from a review of your strategy or training in this area.**

  Investment Uncut - Systemic risk in the financial sector with David Aikman

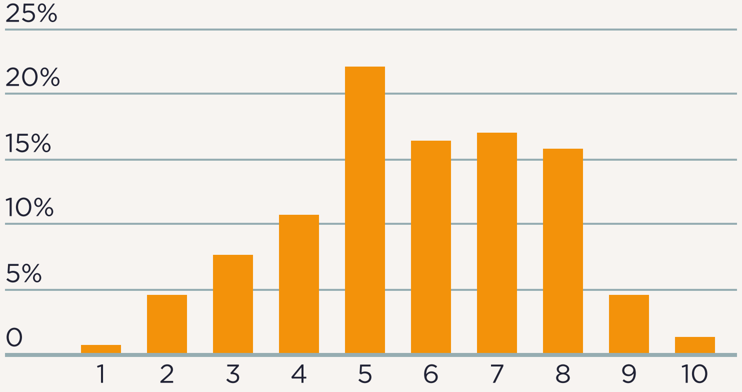
Spotlight on Cyber risk

How much do you worry about cyber risk for your scheme? (1 = not worried, 10 = very worried)



Cyber risk is a growing concern for many schemes and our respondents made that clear in their survey results – with well over half rating their concern about this risk as 7 or more out of 10.

How prepared do you feel? (1 = not prepared, 10 = very prepared)



Results were more mixed when it came to describing how prepared our respondents felt. It is encouraging to see many feel well prepared but others feel they have more work to do in this area. If we look at responses by scheme size, our respondents from larger schemes generally feel marginally more prepared than those from smaller schemes.

What are your specific concerns regarding cyber risk?

We have grouped responses into the themes shown below

Nearly a third of our respondents highlighted data and systems breaches as a specific area of concern which is not unexpected. The uncertainty of the unknown and the ever-evolving nature of cyber risk also ranked highly. Whilst it is not possible to prepare for every eventuality, scenario testing (or wargaming) is a useful way to test actions and behaviours and identify roles and responsibilities for use in a crisis. This preparatory work will be valuable should a cyber or other unexpected incident occurs and can be used as a tool to continuously improve existing incident response plans.

When it comes to cyber risk, we encourage our clients to have a mindset of "when" rather than "if". This encourages positive action to prepare for and reduce cyber risks, as well as putting together a plan to react if and when needed.

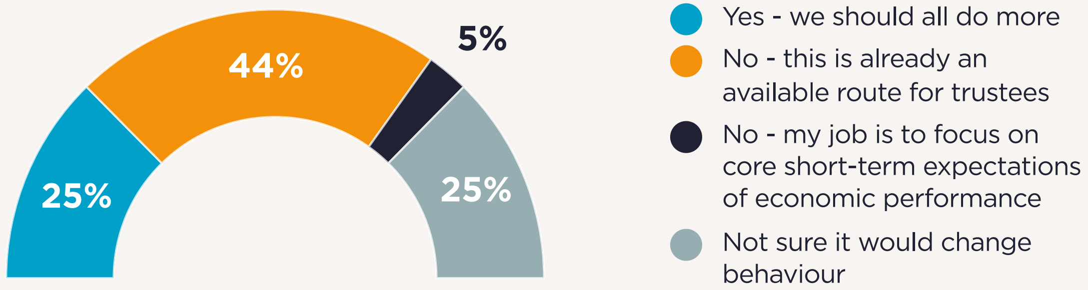
Peter Shaw
Senior consultant, Pensions Management

Curious?

+ **To learn more about actions you should consider, including testing your incident response, get in touch with Peter Shaw and ask to see our cyber security checklist.**

Action on responsible investment and net zero

Would you support a new interpretation of fiduciary duty to enable trustees to consider climate and other systemic risks when making investment decisions?

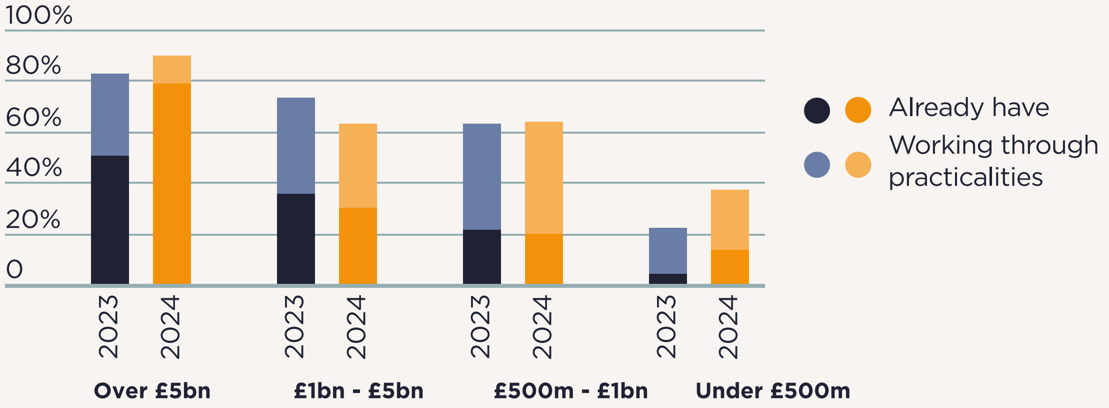


A quarter of respondents said there should be a new interpretation of fiduciary duty to enable trustees to consider climate and systemic risks when making investment decisions, while 44% believe that this is already an available option.

> *As trustees get closer to their endgame, and have taken steps to minimise conventional areas of pension risk, systemic risks such as climate change become a larger share of their scheme's remaining risk exposure. Hence these risks should be on their agenda.*

Claire Jones
Partner and Head of Responsible Investment

Will you be setting a net zero emissions target for your scheme?



Our results also show that the proportion of large schemes (in the over £5bn bracket) that have set a net zero target has increased from last year. For these large schemes, this may be a case of trustees building on the work they are doing to meet their climate reporting requirements. However, the survey also reveals that there has been a significant uptick in the number of smaller schemes (in the under £500m bracket) that have also set a net zero target despite the fact there is no regulatory pressure to do so. There remain many schemes that are working through the practicalities, suggesting that progress in formally agreeing targets can be slow.

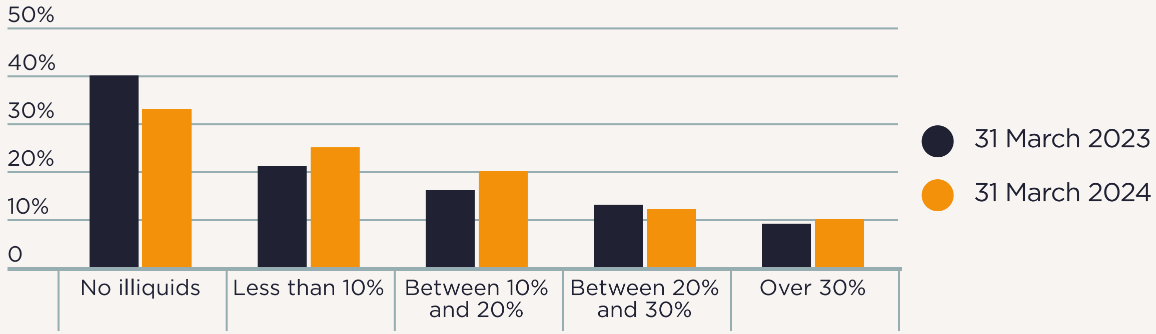
Curious?

+ To learn more about climate risks for pension schemes, read our latest Vista magazine or or find out about Climate change, ESG and sustainable investment here.

Refining investment strategy

Progress on selling down illiquid assets has been limited

Illiquid allocations held by schemes at the beginning and end of the year



Source: LCP Visualise

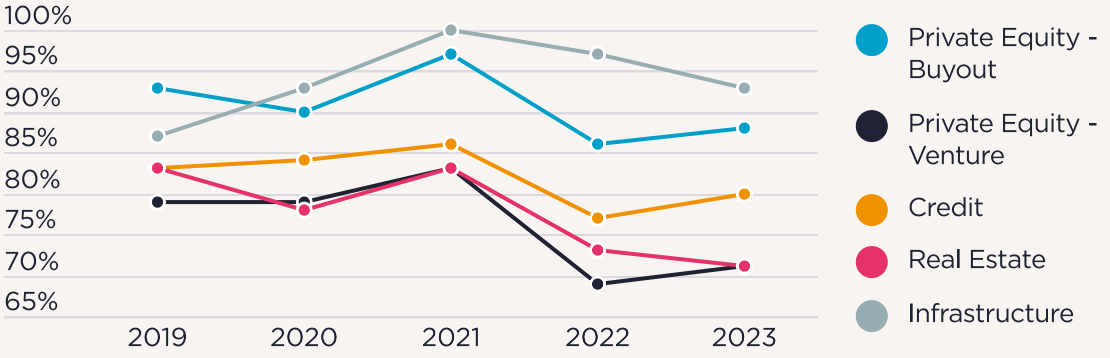
Given the improvements we have observed in funding levels, schemes are reaching their endgame sooner and may then have to navigate a secondary market sale of their illiquid assets in short order. We would encourage any scheme that might face this challenge to start planning early and agree a strategy that dovetails with your wider market approach. In our experience providing illiquid asset solutions to our clients, early engagement as part of a clear exit strategy can lead to improved outcomes.

Illiquid assets present both opportunities and risks to DB schemes, and we are able to offer the strategic support to meet a range of investor objectives.

Nick Cooney
Partner, Investment

Secondary market pricing has seen large discounts in the past couple of years

Price of secondary market assets (as % of NAV)



Source: LCP, Various Secondary Market Advisors/ Brokers, Secondary Buyers. For illustrative purposes only

The level of discounts (as % of NAV) has been driven by a number of factors, but we continue to hear from brokers that one of the most significant is the continued “overallocation” to private assets for many global investors who then decide to sell in short order to achieve greater liquidity. We believe that broker selection is key to finding the right buyers/sellers, and by extension the right price.

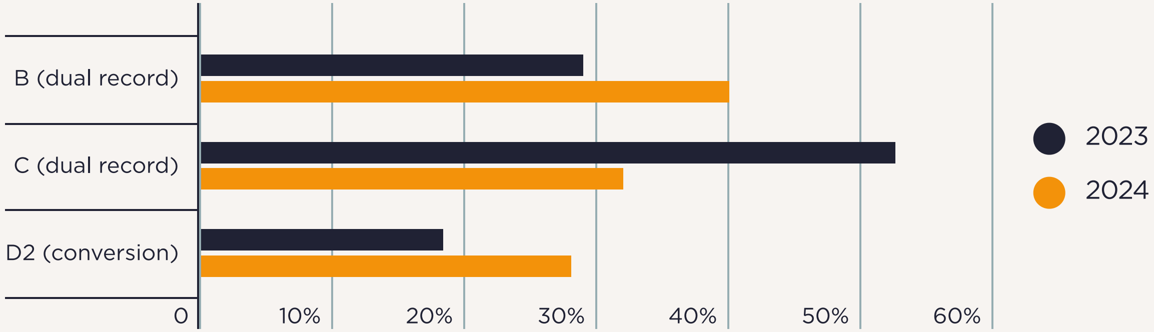
Schemes should think carefully about allowance for haircuts on illiquid assets when looking at current and projected funding positions, especially when targeting insurance - to avoid any nasty surprises.

Curious?

+ To learn more about secondary markets for illiquid holdings read our latest [Vista magazine] or speak to your LCP consultant.

Member focus

Which method have you decided to use (or have you used) to equalise for GMPs for future payments?



Our survey showed that lots more schemes are opting for Method D2 (conversion) or the more generous dual-record Method B ahead of the “default” Method C2 as they start to work through the complexities of equalising GMPs.

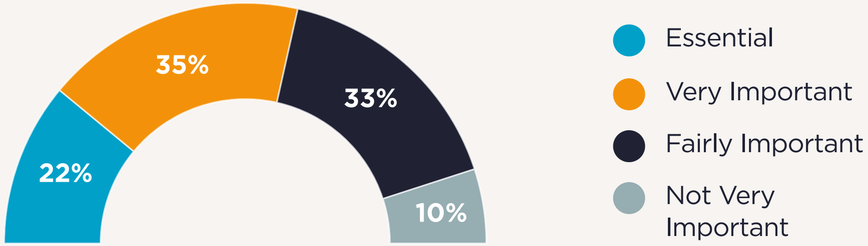
This isn’t a surprise to us – Method B is in theory more expensive than Method C2, but we have found in many cases the extra cost is tiny and outweighed by the relative simplicity and administrative cost savings of Method B.

Method D2, using GMP conversion, can provide wider simplification but is a significant project so there needs to be a clear justification for selecting this method.

Curious?

+ **Hear about the latest GMP insights and learn about how our member options review can improve your members’ experience and accelerate your journey to your endgame.**

How important is it to you that your members have access to a website/app that allows them to accurately model their benefit options?



In past editions of this report we’ve highlighted the win-win-win that a good member options strategy can have: potentially reducing journey-plan timescales, reducing costs and adding real value for members themselves.

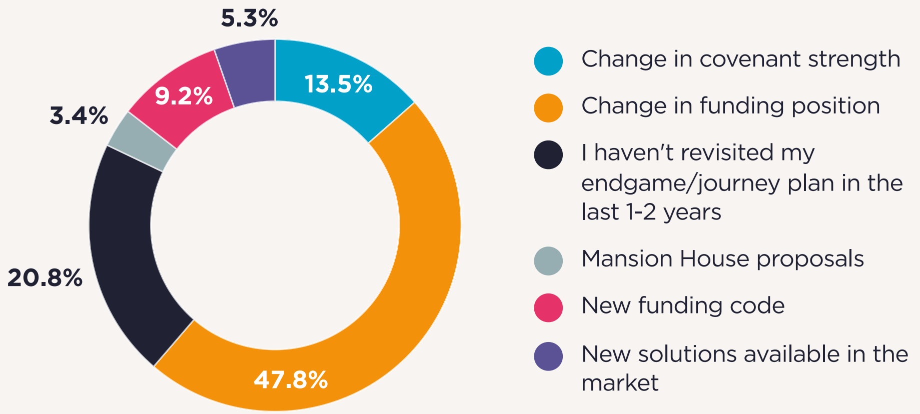
Part of that involves making members aware of their options and helping to understand what they mean – so it was great to see more than half of respondents say they think a website that allows members to model their benefits is either essential or very important. Thinking about the extent to which such options can be introduced or maintained for members is also a key part of endgame strategy discussions.

Providing clear and timely information, together with appropriate options and access to the support needed to make informed decisions is key to ensuring members receive good retirement outcomes.

Clive Harrison
Partner, Actuarial

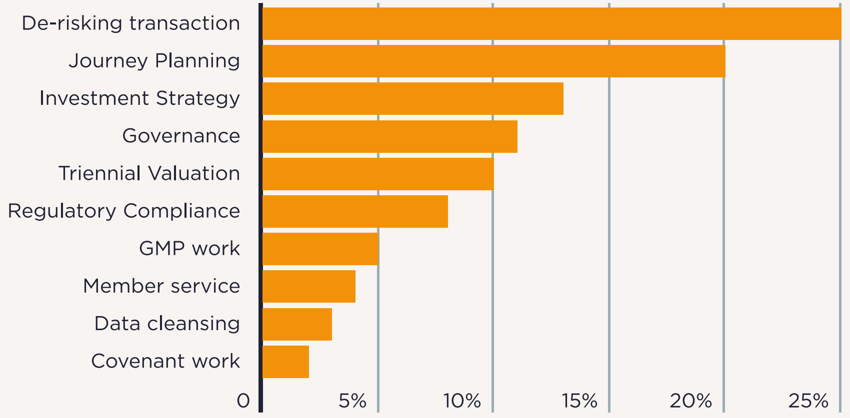
Journey planning and future priorities

If you have revisited your endgame / journey plan in the last 1-2 years, what were the key drivers for this?



Changing funding levels have been the key driver for journey planning activity in recent years. This is not surprising given the gilts crisis sparked by the mini-budget which saw underhedged schemes improve their funding positions in a short space of time. In addition, further recent improvements to scheme funding levels will have reinforced the message to trustees to rethink their journey plan and explore alternative endgames that may not have been previously possible. New solutions in the pensions market, eg superfunds or options opened up by the Mansion House proposals, are not yet a significant driver of strategic change but may be in years to come.

What is your top priority for your scheme in the coming year?



The most-cited priority for respondents in the coming year was to complete a de-risking transaction – understandable given the recent funding improvements. For a large number of other respondents, journey planning and revisiting their investment strategy were priorities, and ones we would endorse. Finally, a number of respondents were using the time to get on top of the governance and regulatory requirements for their schemes.

Curious?

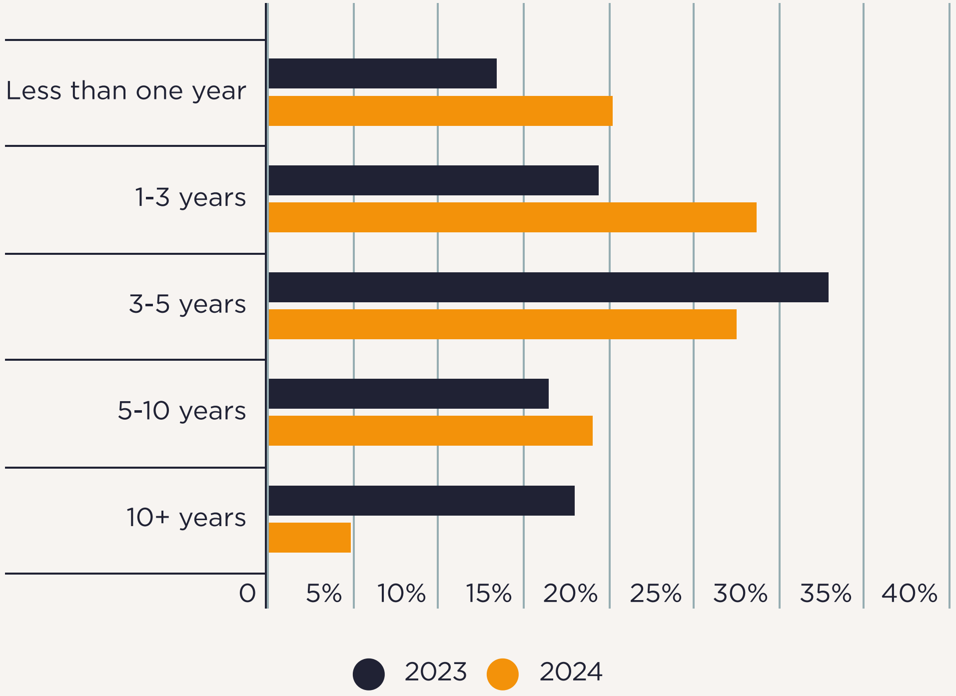
+ Check out our LCP Strategic Journey Planning website hub for more information on revisiting your journey plan.

It is fantastic news that funding has been improving for many schemes, and important for trustees to understand the full range of endgame options available to them in 2024 and beyond.

Chris Potts
Principal & Lead Author

Pensions Risk Transfer – preparation is key

What is the expected timeframe for your final transaction?



For those who are targeting full insurance (c50% of respondents to our survey), the timescales to achieve this have come in significantly compared to last year's responses. The proportion expecting their final transaction to be 10+ years away has fallen sharply, while timeframes of less than 3 years are increasingly common.

Are you intending to use a phased buy-in approach or to insure all liabilities in one go?

Interestingly, despite insurance market dynamics shifting towards full as opposed to partial buy-ins, **more than 40%** of respondents still expect to follow a phased approach to insuring their scheme's liabilities. A similar proportion expect to insure all liabilities in one go, with the rest not yet sure.

A strategic approach to data management

The demand for high quality data has never been more critical, especially when it comes to approaching the insurance market and minimising residual risks post transaction. LCP's **Data Services Team** guides schemes through their data journey on the road to successful risk transfer, beginning with comprehensive data and benefit reviews and continuing through cleanse and rectification – working closely with all stakeholders to achieve an approach which manages risk and provides insurers with the data they value.

Our survey showed that the insurance market is likely to be busy for some time to come – so doing your data, benefits and assets preparation and working with an adviser who knows the market is more important than ever.

Charlie Finch
Partner, Pensions Risk Transfer

Curious?

+ **Learn more about the steps involved in an insurance transaction, as well as latest innovations, on Pensions Risk Transfer.**

Managing the post transaction and wind-up process

Securing all benefits with an insurer is a significant step but is by no means the end of the road. Completing the steps required to move to buy-out and ultimate wind-up of a scheme requires careful management and specialist support. Trustees and sponsors must navigate a complex process with multiple workstreams, while ensuring members feel reassured throughout the process.

The rapid growth in the pensions risk transfer market is putting pressure on administrators and insurer transition teams. Over 200 transactions completed in 2023 and many of these schemes will be looking to wind-up over the next couple of years. Some of the key stages in these complex processes are set out opposite.

Specialist support for the post transaction process is invaluable, providing:

- **Strategic advice on key risk areas –** to support you dealing with some of the challenging issues that can arise around treatment of surplus, discretionary benefits and section 37, and avoiding common pitfalls;
- **Access to strong insurer relationships –** ensuring that your scheme's transition is prioritised in a busy market, you have a detailed understanding of insurer processes, and your members have peace of mind that their benefits are in safe hands; and
- **Active project management -** to drive forward progress and adapt plans appropriately if circumstances change.

In this final stage of a scheme's journey, careful planning and specialist support are key to a successful outcome for trustees, sponsors and members, particularly in today's busy market.

Rachel Banham
Partner and Head of Post transaction team

The stages to completing an efficient wind-up are:

Operational process	Work with your administrators to set up the operational processes between the insurer and administrator during the buy-in phase to ensure continuity for members and minimise the need for subsequent benefit corrections.
Communications strategy	Develop a comprehensive, well planned communications strategy so that members are provided with appropriate information at the right time and the trustees benefit from statutory protections.
Data cleanse	Ensure the timely execution of the data cleanse exercise, including GMP equalisation, and resolve any benefit issues in accordance with a clear actionable plan that meets the insurer's requirements.
Member options and non-core benefits	Consider and implement options for securing members' other benefits eg AVCs, other DC benefits and historical individual annuities which may need to be secured separately outside the scheme. Offer winding up lump sums, where appropriate.
Administration transfer and issuing policies	Effect a smooth transition of administration and pensioner payroll to the insurer while closely managing tax information and making sure that individual policies are issued to members at the right time.
Wind-up and trustee protections	Manage the final tasks such as: triggering the wind-up at the appropriate time, production of final accounts, management of any surplus, completion of the necessary statutory notifications and consideration of appropriate trustee protections beyond the wind-up.

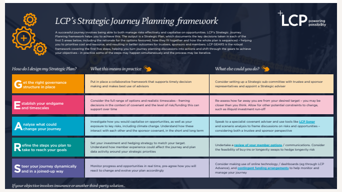
Curious?

+ Our Post transaction team includes over 25 specialists in this area, making it the largest in the market. Get in touch to find out how we can help you to manage the final stages of your pension scheme's journey – whether or not we have been involved to date.

Curious?

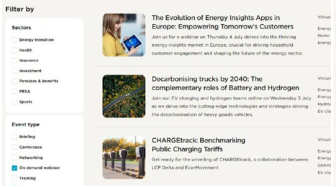
Additional resources to find out more

[LCP Strategic Journey Planning framework]



[LCP Strategic Journey Planning website hub]

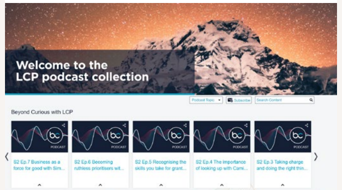
[Our latest webinars, accessed on demand]



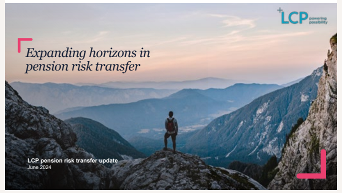
[Trustee DEI guide]

[Professional Corporate Sole Trustee report]

[LCP podcast collection including Investment Uncut]



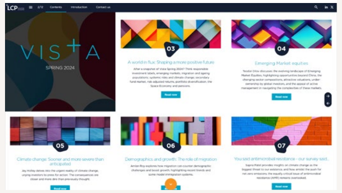
[De-risking update]



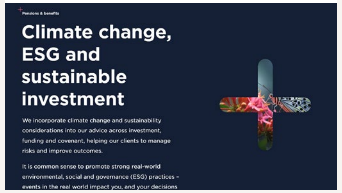
[Longevity report]

[Contingent funding handbook]

[Vista – our investment magazine]



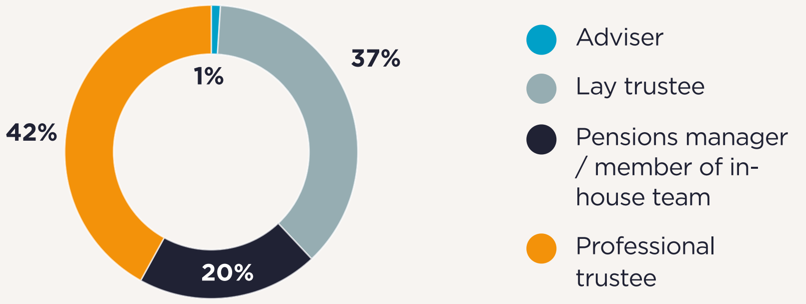
[Climate and sustainability hub]

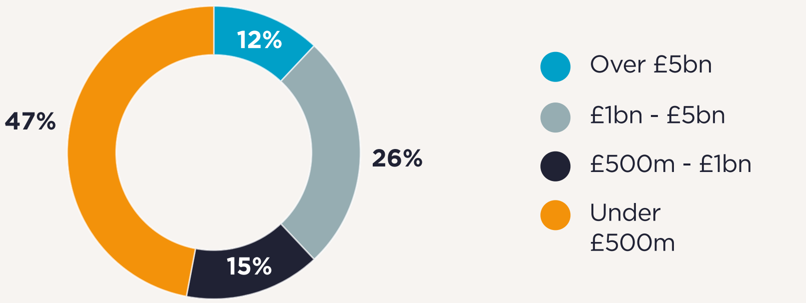


[LCP Beacon]

Our survey

In our latest survey, respondents representing trustees, sponsors, pensions managers and advisers told us about their schemes and gave us their insights on the UK pensions landscape.





What about our client data?

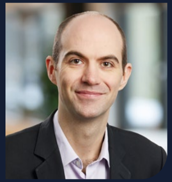
Our data covers over 225 UK DB pension schemes advised by LCP, ranging in size from less than £10m to £15bn and collectively representing around £150bn of assets. This includes schemes where LCP provides actuarial, investment, covenant or corporate advice (or a combination) so does not necessarily represent LCP's advice in all areas.

What did we ask?

1. Are you a professional trustee, lay trustee, sponsor, pensions manager/member of in-house team or adviser?
2. What size is your scheme (asset size)?
3. Do you have a long-term low dependency funding target?
4. What is the long-term objective for your scheme?
   a. If full insurance, are you intending to use a phased buy-in approach or insure all liabilities in one go?
   b. What is the expected timeframe for your final transaction?
5. If you have revisited your endgame / journey plan in the last 1-2 years, what were the key drivers for this?
6. Will you be setting a net zero emissions target for your scheme?
7. Would you support a new interpretation of fiduciary duty to enable trustees to consider climate and other systemic risks when making investment decisions?
8. How long do you think your employer covenant is reliable for?
9. Which method have you decided to use (or have you used) to equalise for GMPs for future payments?
10. Cyber risk:
    a. How much do you worry about cyber risk for your scheme?
    b. How prepared do you feel?
    c. What is your biggest concern surrounding cyber risk?
11. What action are you taking in relation to DEI issues?
12. How important is it to you that your members have access to a website / app that allows them to accurately model their benefit options?
13. Rank these systemic risks in order you are most worried about for your DB scheme: Climate change; LDI leverage spiral; Deflation; Gilt or swap market collapse; Regulatory risk; Longevity step change; Societal upheaval; Cyber / Artificial Intelligence.
14. What is your top priority for your scheme in the coming year?

LCP's Chart your own course team

Please get in touch to find out more



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At LCP, our experts help to power possibility by navigating you through complexity to make decisions that matter to your business and to our wider society. We are powered by our desire to solve important problems to shape a more positive future. We have market leading capabilities across pensions and financial services, insurance, energy, health and analytics.